

Message Text

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PAGE 01 LAGOS 05875 01 OF 02 111248Z

ACTION AF-10

INFO OCT-01 EUR-12 ISO-00 EB-08 XMB-02 /033 W

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FM AMEMBASSY LAGOS

TO SECSTATE WASHDC 8391

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LIMITED OFFICIAL USE SECTION 01 OF 02 LAGOS 5875

E.O. 11652: N/A

TAGS: BENC, ENRG, NI

SUBJECT: MAJOR PROJECT: NIGERIAN LNG

REF: LAGOS 5135

1. PHILLIPS PETROLEUM OFFICIALS BOB NAGEL, CHARLES PURDY AND PAUL TUCKER ARRIVED LAGOS MAY 3 IN CONNECTION WITH PLANNED SIGNING OF SHAREHOLDERS AGREEMENT FOR NIGERIAN LNG PROJECT SCHEDULED TO TAKE PLACE MAY 11. PHILLIPS FACING MAJOR SNAG ABOUT WHICH IT HAD WARNED NNPC, BUT ON WHICH NNPC HAS SO FAR FAILED TO FOCUS. ACCORDING TO SECTION 902 OF U.S. INTERNAL REVENUE CODE, NAGEL SAID, PHILLIPS MUST OWN AT LEAST 10 PERCENT OF EQUITY IF NIGERIAN TAXES ON ITS PROFITS ARE TO BE GIVEN CREDIT AGAINST U.S. INCOME TAXES. PROBLEM DID NOT EXIST WHEN THERE WERE TWO LNG PROJECTS AND PHILLIPS WAS 15 PERCENT SHAREHOLDER IN ONE OF PROJECTS WITH NNPC, AGIP AND ELF. HOWEVER, MERGING OF TWO PROJECTS INTO ONE BY FMG REDUCED EACH PARTNER'S SHAREHOLDING BY HALF, SO PHILLIPS NOW HAS ONLY SEVEN AND ONE-HALF PERCENT.

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PAGE 02 LAGOS 05875 01 OF 02 111248Z

2. LOSS OF CREDIT FOR NIGERIAN INCOME TAX PAYMENTS WOULD CUT PHILLIPS NET AFTER TAX PROFITS ALMOST IN HALF. UNLESS PHILLIPS CAN OBTAIN AN ADDITIONAL TWO AND ONE-HALF PERCENT EQUITY, COMPANY WILL HAVE TO REFUSE TO SIGN SHAREHOLDER'S AGREEMENT. UNFORTUNATELY, COMMISSIONER OF PETROLEUM BUHARI, NNPC MANAGING DIRECTOR MARINHO, AND NNPC GAS MAN AKPE, TOGETHER WITH OTHER NNPC OFFICIALS, HAD JUST LEFT FOR OPEC CONFERENCE IN TAIF ON MAY 3.

PHILLIPS OFFICIALS HAD ONLY A FEW MOMENTS TO HAND MARINHO A PAPER ON PROBLEM BEFORE HIS DEPARTURE AND WERE CONCERNED THAT BUHARI AND MARINHO WOULD NOT BE ABLE TO FOCUS ON ISSUE BEFORE RETURNING TO LAGOS MAY 9. BY THEN, IT WOULD BE TOO LATE TO DISCUSS POSSIBLE REMEDIES IN TIME TO SIGN SHAREHOLDERS AGREEMENT.

3. NAGEL WILL SUGGEST TO MARINHO THAT EITHER NNPC SHOULD SELL TWO AND A HALF PERCENT OF ITS SIXTY PERCENT SHAREHOLDING TO PHILLIPS, OR ALTERNATIVELY NNPC SHOULD OBLIGE AGIP TO SELL PHILLIPS THE NECESSARY PERCENTAGE. AGIP IS THE LOGICAL CHOICE TO ASK TO SELL PART OF ITS EQUITY, NAGEL SAID. NEITHER SHELL NOR BP CAN REDUCE THEIR TEN PERCENT HOLDINGS SINCE BRITISH TAX LAWS IMPOSE THE SAME CONDITIONS AS IRC SECTION 902. IT IS UNDERSTANDABLY DOUBTFUL THAT ELF WOULD BE INTERESTED IN HOLDING LESS THAN ITS PRESENT FIVE PERCENT STAKE. ON THE OTHER HAND, AGIP SHOULD NOT MIND BEING REDUCED TO THE SAME SHAREHOLDING AS ELF. NEITHER FRANCE NOR ITALY INTENDS TO BUY NIGERIAN LNG, AND THERE IS NO ADVANTAGE TO BE GAINED ON BEHALF OF ITALIAN CONTRACTORS OR EQUIPMENT SUPPLIERS BY VIRTUE OF AGIP HANGING ON TO A LARGER SHAREHOLDING. HOWEVER, NAGEL SAID PHILLIPS DOES NOT WANT TO APPROACH AGIP DIRECTLY REGARDING SALE SINCE AGIP WOULD SCENT AN OPPORTUNITY TO DRIVE A HARD BARGAIN.

4. PHILLIPS OFFICIALS ASKED IF EMBASSY COULD SUGGEST ANY ACTION THEY OR WE MIGHT TAKE PRIOR TO RETURN OF BUHARI AND MARINHO TO BRING PROBLEM TO THE ATTENTION OF APPROPRIATE LIMITED OFFICIAL USE

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PAGE 03 LAGOS 05875 01 OF 02 111248Z

AUTHORITIES AND GET A READING ON WHAT FMG RESPONSE LIKELY TO BE. ECON COUNSELOR RAISED MATTER WITH MOI PERMSEC ALHAJI ABUBAKAR, WHO SAID HE PERSONALLY THOUGHT PHILLIPS HAD A GOOD ARGUMENT BUT THAT FINAL DECISION UP TO BUHARI.

5. ASIDE FROM POSSIBLE EQUITY STUMBLING BLOCK, NAGEL SEEMED RELATIVELY OPTIMISTIC ABOUT PROGRESS ON LNG PROJECT. PHILLIPS, HE SAID, HAS HELD TALKS WITH FOUR POTENTIAL CUSTOMERS IN U.S. THREE OF THEM ALREADY HAVE RECEIVING TERMINALS, WHILE THE FOURTH IS APPLYING FOR APPROVAL TO CONSTRUCT ONE. THEY ALL NEED GAS SUPPLIES, HAVE PIPELINES, AND ARE PREPARED TO MOVE QUICKLY. NAGEL SAID ROUGHLY HALF OF THE LNG EXPORTED TO THE U.S. WOULD BE DELIVERED TO THE GULF OF MEXICO TO SUPPLY CONSUMERS IN THE MIDWEST, WHILE THE OTHER HALF WOULD GO TO U.S. EAST COAST.

6. NO PRICES HAVE YET BEEN SET FOR EITHER RAW GAS OR FINISHED LNG. HOWEVER, NAGEL SAID, NNPC HAS OPENED NEGOTIATIONS WITH OIL COMPANIES WHO WILL PRODUCE GAS AND CANNOT BE ACCUSED OF

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PAGE 01 LAGOS 05875 02 OF 02 111253Z

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LIMITED OFFICIAL USE SECTION 02 OF 02 LAGOS 5875

FOOTDRAGGING ON THAT SCORE. COMPANIES HAVE BEEN SHOWN "GAS PROFILE" PREPARED BY IMEG WHICH INDICATES THE LOCATION OF FIELDS WHERE FMG OWNED GAS GATHERING COMPANY WILL BEGIN COLLECTING GAS AND THE SEQUENCE IN WHICH IT WILL TAP THEM. GAS GATHERING WILL BEGIN WITH MAJOR STREAMS OF ASSOCIATED GAS PRESENTLY BEING FLARED. COMPRESSORS USED WILL BE PORTABLE SO THEY CAN LATER BE MOVED TO WORK ON NON-ASSOCIATED GAS FIELDS. FMG WANTS RECOGNIZED INTERNATIONAL GAS TRANSMISSION COMPANY AS 15 PERCENT PARTNER IN GAS GATHERING COMPANY AND HAS CONTACTED SUCH FIRMS IN U.S., JAPAN, EUROPE AND CANADA. HOWEVER, NAGEL OBSERVED, MOST GAS TRANSMISSION COMPANIES HAVE THEIR HANDS FULL PLANNING CAPITAL INVESTMENTS IN THEIR OWN COUNTRIES AND WOULD SEEM TO HAVE LITTLE INCENTIVE TO SHOULDER THE ENTIRE BURDEN OF OPERATING A TRANSMISSION GRID UNDER DIFFICULT CIRCUMSTANCES IN AN UNFAMILIAR COUNTRY FOR A MERE 15 PERCENT. MOREOVER, THOSE U.S. FIRMS WHICH HAVE EXPRESSED ANY INTEREST WANT TO MAKE THEIR INVESTMENT CONTINGENT UPON ASSURE LNG SUPPLIES, WHEREAS THE FMG WOULD PREFER TO KEEP ITS HANDS UNTIED IN ORDER TO SHOP AROUND FOR THE BEST OFFER BEFORE COMMITTING ITSELF TO CUSTOMER.

7. NAGEL ESTIMATED THAT CONSTRUCTION COULD BEGIN FROM 12 TO 15

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PAGE 02 LAGOS 05875 02 OF 02 111253Z

MONTHS AFTER SIGNING OF SHAREHOLDER'S AGREEMENT PROVIDING THERE ARE NO DELAYS IN FERC APPROVAL. HE SAID APPLICATION COULD BE READIED FOR SUBMISSION TO FERC BY END OF 1978. ASSUMING SHARE-

HOLDER AGREEMENT IS SIGNED IN MAY OR JUNE, CONSTRUCTION COULD
THUS BEGIN THIRD QUARTER 1979. THIS WOULD LEAVE SIX TO NINE
MONTHS FOR FERC REVIEW AND APPROVAL OF APPLICATION, WHICH
IS OPTIMISTIC IN VIEW OF PAST EXPERIENCE. NAGEL OBSERVED THAT
FERC WILL HAVE DIFFICULTY TAKING ANY ACTIONS UNTIL ENERGY BILL
IS PASSED. FOLLOWING FERC APPROVAL AND BEGINNING OF CONSTRUCTION,
FIRST TRAIN OF LNG PLANT COULD BE COMMISSIONED IN 35 MONTHS.
ADDITIONAL TRAINS COULD BE COMMISSIONED EVERY TWO TO THREE MONTHS
THEREAFTER. NAGEL SAID PHILLIPS PLANS TO USE MODULAR CONSTRUCTION
WITH UNITS OF ABOUT 1,000 TONS EACH FABRICATED ON THE U.S.
GULF OR EAST COASTS, OR IN FRANCE OR ITALY (ANYWHERE, HE SAID
EXCEPT IN BRITAIN).

8. COST OF ENTIRE PROJECT MAY BE CLOSE TO DOLLARS 6 BILLION.
GAS GATHERING GRID WILL COST BETWEEN DOLLARS 500 AND 800 MILL-
ION. LNG PLANT ITSELF IS DOLLARS 1.8 BILLION, AND 15 TO 18
LNG TANKERS WILL BE NEEDED AT DOLLARS 184 MILLION EACH. NAGEL
SAID HE HAS DISCUSSED LNG PROJECT WITH EXIMBANK. LNG PLANT IT-
SELF COULD INVOLVE FINANCING DOLLARS ONE BILLION IN U.S. MATER-
IALS AND EQUIPMENT. IF RULE STILL IN EFFECT THAT HALF OF GAS
IMPORTED INTO U.S. MUST BE CARRIED IN U.S. BOTTOMS, TANKERS COULD
ADD ANOTHER 1.5 BILLION. CONSTRUCTION AWARD, IF WON BY U.S.
CONTRACTOR, WOULD ALSO BE SUBSTANTIAL. IF EXIMBANK MAKES A LOAN,
BONNY LNG, WHICH IS 60 PERCENT FMG OWNED, WOULD BE GUARANTOR,
WITH EXIMBANK IN EFFECT HAVING CHATTEL MORTGAGE ON BONNY'S
ASSETS.
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